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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

No. 359.

STOCKHOLDERS' COMMITTEE OF THE UNIVERSAL LUBRICATING SYSTEMS, INC.,
Petitioner,

vs.

AUSTIN L. STALEY, Trustee in Reorganization for the Universal Lubricating Systems, Inc.

PETITION FOR REHEARING OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

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(a) The purpose of the reorganization act to be to continue business through existing stockholders;

(b) The public necessity for such continuance in the constant need of operating capital; and

(c) The methods by which to attain this most necessary result.

So, as a result, there is aligned on the side of Petitioners, representing the stockholders, Congress, with its declared purpose to save them, and the great purpose to avoid and to minimize the effect of depressions, making this a major conservation measure 6

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Congress has not stopped at declaring its purpose as to reorganizations in a report and by pass-

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III.

Petitioners rely on their original brief for the Statement of Facts and their Argument as to the merits of the case as a private one between the parties, and will refer only in the briefest way here to those matters.

The decision of the Court below is in direct and irreconcilable conflict with the purpose of reorganization as declared by Congress and should be reversed for that reason and in the public interest, —to minimize and repel depressions, to secure capital to enable factories to operate, and to keep labor employed,—none of which is given any consideration by the Court below.

The decision below is in conflict with the findings and the evidence, and its decision is injust and inequitable, and certain of its provisions are in conflict with basic law. For these reasons also the decision below should be reversed 1

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PETITION FOR REHEARING OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable, the Chief Justice of the United States and Associate Justices of the Supreme Court of the United States:

Petitioner, a Stockholders' Committee, respectfully request a rehearing and a reconsideration of their Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Third District, which was denied by this Court on October 8, 1945.

Statement.

Petitioner respectfully asks a rehearing herein on the ground that a paramount public interest is involved to which, because unaware of it, reference was not made in the original petition, a lack of knowledge, however, shared apparently by all other members of the bar, as counsel is unable to find any reference to it in other briefs,—and so the Court, through its not being urged, has never referred to it in its decisions, so far as counsel is able to find.

The case is one arising under the reorganization provisions of the Bankruptcy Act. The question at issue is whether the debtor is solvent. The Court below found, wholly in conflict with the evidence, that it is insolvent and excluded the stockholders from participation in the new corporation.

The broad, general purpose of the reorganization act is to avoid depressions, minimize them when they exist, save stockholders and investors, and keep labor employed. The act has been so interpreted by the Congress, and its construction should be the controlling factor in the decision of reorganization cases. This intent of Congress to save business instead of liquidating it,—to keep it in the hands of stockholders trained for management and skilled through experience, instead of turning it over to security holders who are merely investors and untrained and inexperienced, —was of vital importance in the prolonged and extreme depression immediately preceding the late war, and will be of equal value and importance in the present reconstruction period when we are to have, as it is estimated, 8,000,000 men temporarily, indefinitely unemployed.

So, Congressional construction of the act is that it should be interpreted and applied to continue business instead of

liquidating it, and to protect stockholders who have gone through prolonged depressions by enabling them to hold on till the prosperous days which Congress feels are sure to come.

In this major effort to protect against and to relieve from depressions the Courts play a necessary and most important role. While, generally, they decide only questions between private parties, here they have the rare and great opportunity and duty to render a great service to the country as a whole.

The views expressed by counsel are not simply his own but are based on the debates on the Chandler Act in the Senate and House, and on the report of the House Committee, and on debates in the House on the Hobbs Bill to more efficiently protect stockholders in railroad reorganizations,—the principles covered by the debate and report being equally applicable to other corporations being reorganized.

We quote at some length from the Congressional debates and report.

Debtor manufactured lubricating appliances but met persistent opposition to marketing by Stewart-Warner, which from 1932 to 1941 brought many patent suits against it, all of which have been determined favorably to debtor. The losses of debtor amounted to $2,000,000 (Ap. 92 a, 93 a, 125 a, 130 a). Afterwards, in May, 1936, debtor obtained loans from one Brynoldt, agreeing, if the loans exceeded $20,000, that all its property should be transferred to Brynoldt. In 1937 the indebtedness exceeded $20,000, whereupon Brynoldt claimed title and exacted a bill of sale and a lease by debtor for three years and eleven months

at $500 per month (Plan p. 49). The property claimed is practically the same as that which the Master found worth $327,000. Brynoldt sought to acquire besides a patent worth $40,000 and common and preferred stock. The Trustee believes there is but remote possibility that Brynoldt could sustain his claim to absolute ownership (July Master's Rep., hereinafter called M. R., para. 25).

The issue herein is whether debtor is solvent. The evidence was as follows:

Two valuations of part of debtor's physical assets were made,—the stockholders' valuation being $325,078.59, and the Trustee's $279,719.20.

The Master found the value $300,000 (July M. R. pp. 25 a, 26 a). From July to October debtor's physical assets increased $27,000 (Oct. M. R. pp. 60 a, 61 a). The claims admitted by the Trustee amount to $397,927.61.

The debtor has a suit for damages against Stewart-Warner for unfair competition, the facts as to which are stated and discussed under 5 of point III, herein-below.

The debtor also claims damages against Brynoldt for his unfounded claim of title to its property, thereby destroying its credit.

The Master and the Courts below have refused to value a coupler patent worth $40,000, paper title to which Brynoldt obtained in his effort to convert his loan into a title.

The Master, trial court and court below have refused to value Universal on earnings, the facts as to which are stated and discussed also under point III herein below.

The results from Trustee's operation of the business have been,—profits May, 1941 to September, 1944—$196,625; for 1943—$151,008.42; for 1944—$124,046.56.

New machines which have been installed to the extent of 40% and will be completely installed which will produce 5½ times as much material, at no added cost, as the obsolete machines.

The debtor's cash position and increase in assets are also stated and discussed under point III, herein below.

The Master allowed Brynoldt's invalid rental claim of $29,316. Taking this and the $40,000 value of the patent into account, the admitted claims and the physical assets, (aside from Stewart-Warner claim), are practically equal.

The Court below found debtor insolvent.

Debtor has 35,000 shares of common stock, at par value of $1.00 per share, and 2150 shares of preferred stock, at par value of $100 per share (Plan p. 5). The reorganized company would have 4,000 shares of preferred stock, at no par value, and 15,000 shares of common stock, at no par value (*id.* p. 11).

Brynoldt, including his invalid rental claim, was found to have a total claim of $71,011.35 (Ap. 23 a), for which he is to receive $35,000 in cash and the balance in preferred and common stock (Ap. 22 a, 23 a, 24 a), and the new company is to have seven directors, including Austin L. Staley, the present Trustee, whose brother is the son-in-law of Brynoldt, Christian Brynoldt and Henry Bergstrom, his attorney (Plan p. 14).

The creditors are to receive one share of preferred capital stock of the new company for each $100 of their claims, plus one share of common stock (Plan p. 20).

The District Judge affirmed the Master's report, except that he directed that the proceeds of the Stewart-Warner litigation be paid to the reorganized company to the amount needed to retire its preferred stock,—the balance to be distributed among debtor's present preferred and common stockholders (Ap. 132 a, 133 a).

REASONS FOR REHEARING.

I.

As a result of the declaration by Congress of the necessity of saving the common stockholder to insure the continued operation of existing corporations and to bring about the organization and operation of new companies, through the furnishing of the necessary capital (which will not be supplied if court decisions unnecessarily and, still more, arbitrarily wipe out common stock investment), this proceeding is demonstrated to be not simply a private one between parties but one where the Congress has declared,

(a) The purpose of the reorganization act to be to continue business through existing stockholders;

(b) The public necessity for such continuance in the constant need of operating capital; and

(c) The methods by which to attain this most necessary result.

So, as a result, there is aligned on the side of Petitioners, representing the stockholders, Congress, with its declared purpose to save them, and the great purpose to avoid and to minimize the effect of depressions, making this a major conservation measure.

(*a*) ***Congress has repeatedly, clearly and most emphatically declared that the purpose of the reorganization act is to continue and not to liquidate business,—to save the investment of the common stockholder, as being in the public interest.***

"The public has an interest in saving a valuable business * * *." (Mr. Chandler, Congressional Record ((hereinafter called C. R.)) Aug. 10, 1937, p. 1189.)

"The theory now is to conserve rather than liquidate the estate, giving the debtor a chance to work out his financial difficulties and not destroy his business. * * * 'It' (bankruptcy) 'means that when financial evil days come upon one, he may seek the aid of the bankruptcy court of the United States and by this method may keep his creditors at bay until he has had time to gain his financial equilibrium. Possibly he may remain in possession * * * until his creditors are brought to a realization * * * that * * * it is better for the bankrupt and for the country if the bankrupt is permitted to continue in his business * * *.' (Michener, a member of the Committee, *id.*)

"A striking characteristic of the amendatory acts which were passed after 1932 was that they were all passed upon a desire to preserve business and to prevent liquidation as far as possible. The old theory * * * was that when the debtor, * * * entered the bankruptcy court his assets were to be marshaled for the benefit of his creditors. He surrendered everything he had, went out of business and then sought to rebuild his fortune as best he could in some other line.

"However, with changing circumstances, * * * it became obvious to those who were administering the bankruptcy laws or practicing under them, to those who were seeking to rehabilitate business, that a different form of procedure was essential.

"On March 3, 1933, there was enacted what is now chapter VIII of the bankruptcy law. This was the first effort to make it possible for a debtor to pay his debts upon the installment plan, as it were, and to continue in business instead of going into liquidation." (O'Mahoney, C. R. Senate, June 10, 1938, p. 8680.)

"You need no better illustration of the importance of the railroads", (and equally the manufacturers), "to the public than the job that has been done by the railroads of this country", (and equally by the manufacturers), "since the war,—not only the so-called solvent railroads", (or manufacturers), "but those * * * undergoing reorganization * * *." (Reed of Ill., C. R. Feb. 14, 1945, p. 1123, Committee member.)

"It is strange * * * that the Commission, * * * has not recognized the importance to the public of protecting the existing investment, and it is even stranger that the courts have permitted the Commission to get away with it. (*id.* pp. 1124-5.)

"The purpose of the Bankruptcy Act, particularly of sec. 77, was to relieve debtors of some of their burdens, not of all of their property.

"The passage of this bill is necessary *now* in order to save the equities owned by thousands of *bona fide* owners of railroad", (manufacturing), "stock and junior bonds. It is also necessary now if we would save railroad", (manufacturing), "credit, without which railroad", (manufacturing), "service in the post-war period will be seriously impaired." (Hobbs, C. R. Feb. 14, 1945; p. 1126.)

"I feel that this bill is in the public interest.

"* * * the court should have a larger part in the review of these cases than they have had under the interpretation of the Supreme Court. This will give it to them, and, in my opinion, represents a just remedy." (Kefauver, *id.* p. 1127, Committee member.)

(b) The Congress, too, has pointed out as the reason for preserving the investment of the common stockholders that existing corporations constantly need new capital for expansion and new corporations to enable them to start, and if common stockholders' investments are unnecessarily destroyed the supply of capital necessary to enable the corporations to operate will not be furnished,—labor will not be employed and depressions will be accentuated instead of being minimized.

"* * * yet in nearly every plan which it," (the Commission), "has brought out it has defeated it's purpose by wiping out the stocks, and thereby forever destroying the market for railroad stocks as investments." (Reed of Ill. C. R., Feb. 14, 1945, p. 1125.)

"We must have railway credit to enable our transportation system," (our manufacturing), "to maintain itself * * *. In war it has been the first line of defense for without transportation" (equally without manufacturing) "there would have been no material sent to the army * * *." *(id.* p. 1125.)

"National need of adequate railway," (manufacturing), "service requires the protection of the investment of both Wall Street and Main Street in railway," (manufacturing), "securities."

"Security must mean complete assurance for the high-priority mortgage-bond investors, and at least reasonable assurance for the investors in common stock and bonds of lower priorities. Otherwise fewer, (factories),railroads will run and those that run will operate inadequately. Each of these deplorable results means fewer jobs for railroad," (manufacturing), "men and lower wages for labor as well as management." (Hobbs, C. R. Feb. 14, 1945, p. 1126.)

"If the transportation system" (the manufacturing) "of a country is to be adequately financed, investment in railroad" (manufacturing) "securities must be kept attractive for private investors. It is folly to expect investors to finance new railroads" (new manufacturing) "by purchasing stocks or junior securities which may be arbitrarily eliminated." (Report 48, 79th Cong. 1st Ses.)

"We cannot have a transportation system" (or manfacturers), "in these United States unless we show some willingness to protect the man who puts his money into it, not merely the banker * * * on the bonds, but the little fellow who buys the stock. We must keep the railway" (manufacturing) "investment attractive for stockholders. It is folly to expect them to finance new

railroad" (manufacturing) "capital by wiping out the investments they have already made." (Reed of Ill., C. R. Feb. 14, 1945, pp. 1124-5.)

(c) The Congress also points out the procedure to be followed to protect the common stock investor in the consideration of evidence and in the provisions of the judgment,—holding that value must be determined on earnings and that the earnings should not be not simply those of the late depression period but that present and prospective earnings should be given due weight, and that in the final judgment or order the common stockholder can and should be given no-par new stock which would be in no way detrimental to security holders with prior rights, as this new stock would be without dividends in years when not earned but would pay dividends in prosperous years.

"One of the elements of this valuation was required to be due consideration of the earning power of the property, past, present, and prospective, and all other relevant facts." (Reed of Ill., C. R., Feb. 14, 1945, p. 1123.)

"It never was intended that these depression earnings should be used as a measure of earning power, and, therefore, a measure of value."

"What is the result? In considering past, present, and prospective earnings, the Commission has put the accent, not on the past earnings, but on the depression earnings, and has failed to temper its judgment by any fair conception of prospective earnings." *(id.* p. 1124.)

"If the earnings are there, the new no-par stock will get it. It cannot harm the bondholder, who is secure in his earnings and who is paid in full before the stockholder participates." *(id.* p. 1125.)

In order to carry out the policy, however, of having fixed interest charges reduced, the bill contains a proviso in sec-

tion 1 (ii) that, if the existing capitalization is in excess of the value of the debtor's property as certified by the Commission under subsection (e)—that is, of what the Commission terms "capitalizable value"—the excess shall be represented by no-par stock issued at the rate of one share for each $100 of such excess. The purpose of this is to afford to the existing stockholders and junior security holders a continued interest in the property. This no-par common stock will still represent actual investment in the property and will still represent a value which the Commission itself has determined under section 19a. It will in no sense be a speculative medium. In bad years, it will pay no dividends; in the good years it should reap the benefit of prosperity at least sufficient to compensate for what the investor has lost in the bad years. As the matter stands now, the investor has suffered through the bad years, and when prosperity has returned the procedure under section 77—originally designed as an act for the relief of debtors—has taken his investment and turned it over to his creditors. (Report #48, 79th Cong. 1st Session, pp. 6 & 7.)

(d) The Congress has further declared as the reason for providing the existing common stock investor with new no-par common stock that it believes that this country will be prosperous and that our application of this act should be on the basis that it will be prosperous, and that the common stockholder, who has gone through a long period of depression, should share in that future prosperity.

> "We recently went through the worst kind of a depression this country had ever seen and, naturally, a good many of the railroads" (and manufacturers) "went through bankruptcy. We are now on the mend. During the last few years the railroads" (and manufacturers) "have had pretty good earnings. If the stockholders are given a chance to hold on to their securities and not be wiped out, they will have an opportunity to get something back out of their investment."

"The railroads" (and manufacturers) "are going to do pretty well in this country for several years to come; and if a stockholder who has common stock can hold it, he has a good chance of getting back some part of his money at least. I am, therefore, in favor of the pending bill and urge its passage." (Gorski, C. R. Feb. 14, 1945, p. 1127.)

"* * * unless we are to admit that our efforts at readjustment after the war will be a failure, then we must insist that the owners of these securities now being confiscated should share in the prosperity which has come as a result of the war and in that which necessarily will follow in rebuilding the Nation's industries." (Report 48, 79th Cong. 1st Session.)

(e) This Court recently, in Otis & Co. v. Securities Exchange Comm., 89 L. Ed. 460, allowed common stockholders to participate in reorganization, based on prospective earnings for fifteen years wiping out $38,700,000 accumulated preferred dividends and furnishing dividends for the common stock thereafter,—an extremely liberal application of the protection Congress has said should be extended to common stockholders, but not stated to be based on the Congressional construction of the purpose of reorganization.

(The two opinions by Justice Reed and Chief Justice Stone are models of logic and literature. The question naturally arises whether the conflicting opinions of these two great Justices would not have been reconciled if the debates in the House and Senate and the Report of the House on reorganization had been called to their attention. However this may be, the considerate treatment of the common stockholders was sustained, which helps greatly to sustain the declared purpose and intent of Congress.

II.

Congress has not stopped at declaring its purpose as to reorganizations in a report and by passage of the House bill and in debates, but has formed a special committee to study the needs of and to promote the prosperity of small business, and has provided as well for making necessary loans to it. This committee has been tireless in its efforts to aid small business, but the cooperation of the courts is necessary to make its measures effective, and the decision below is extremely harmful to the Congressional purpose and efforts.

Debtor's business is a small one and Congress has not stopped in its efforts to aid small business at reports and debates and passing the House bill, but it has formed a special committee, called a "Select Committee to Investigate and Study Small Business," which has been as active as any committee in Congress in investigating and studying methods and means to promote and protect small business. In this effort it has issued weekly detailed accounts of its proceedings and of its resultant recommendations, and has provided an organization and the funds to make loans to them. Congress has made it plain that it regards small business as the backbone of the prosperity of the country and has demonstrated in every way its desire to protect and encourage it.

To make these efforts of Congress successful, the active, continuous, wholehearted support of the courts is necessary, without which the efforts of Congress can be helpful in only a very limited way. To give real effect to the beneficial purpose of Congress the wholehearted, continuous and tireless cooperation of the courts is necessary.

The decision below is a serious blow to the helpful efforts of Congress.

III.

Petitioners rely on their original brief for the Statement of Facts and their Argument as to the merits of the case as a private one between the parties, and will refer only in the briefest way here to those matters.

The decision of the Court below is in direct and irreconcilable conflict with the purpose of reorganization as declared by Congress and should be reversed for that reason and in the public interest,—to minimize and repel depressions, to secure capital to enable factories to operate, and to keep labor employed,—none of which is given any consideration by the Court below.

The decision below is in conflict with the findings and the evidence, and its decision is injust and inequitable, and certain of its provisions are in conflict with basic law. For these reasons also the decision below should be reversed.

(a) The decision below fails utterly to take into consideration the public nature and need of the reorganization statute. On the contrary, it emphasizes throughout stated but unreal objections to the stockholders sharing in the reorganized company, and fails to consider the facts showing them entitled to share.

(b) The refusal of the Court below to value debtor's property on earnings was in conflict with declared purpose of Congress, ((c) of Pt. 1 above), and with the Master's findings, and the evidence, as approved by the trial court,

and the grounds of the refusal are not sustained by any evidence, and the Court below was without jurisdiction to reverse the findings.

The grounds of the decision of the Court below on which it refused to value on earnings are stated by it as follows,—

1. "As to the years prior to the trusteeship, the special master stated that the losses may have been due to litigation with Stewart-Warner, though he did not so find as a fact." (Opinion, p. 5.)

This omits the following additional and conclusive facts:

"* * * litigation, extending over a number of years, has occasioned the expenditure of a great amount of money for incidental expenses and counsel fees, and losses of various kinds, * * * in that litigation * * *." (Trustee's Plan, top p. 4.)

"I believe defendant had suffered the amount of damages claimed in the amended counter-claim." ($2,000,000) (Appendix 130 a.)

2. The Court held,—

"We heard a great deal of argument about good prospects for the business. * * * All of this may well be true and we hope, for the sake of those engaged in the enterprise, that it proves to be true. It bears upon the question of the feasibility of any plan which contemplates the continuance of the debtor as a going business concern. But such prospects do not furnish an argument for capitalization of earnings to show present worth when the earnings have come under the highly artificial stimulus of war production and an unusually favorable tax situation." (Opinion, p. 5.)

So, its decision below was ultimately reached on two grounds,—that the findings as to the prospects and outlook of debtor must be overlooked because part of debtor's production had been war work, and because debtor had an unusually favorable tax situation.

The ruling that the prospects and outlook of the debtor could not be considered ignores the five special findings of the Master, based on undisputed evidence, that

> "there will be a great and increasing need of lubricating devices * * * manufactured by debtor";
> that "a modern plant would be built up which would have a small but profitable business and be able to compete with any competitor at any price";
> that "The evidence shows grounds for expecting success for the reorganized company if it has adequate working capital";
> that "The prospects for the entire line of fittings * * * are a great deal brighter than they were at * * * previous hearings";
> and that "* * * if there is a prompt reorganization and building up of the key personnel the company will have profitable operations to such an extent as to be able to maintain dividends on the preferred stock and possibly pay it off over a period of years." (Committee's original brief, p. 4.)

The Court below also ignored the testimony of the expert witness.

These findings and the evidence conclusively show that the reorganized company will have far more business than the debtor had in war time, and that it will be a seller's not a buyer's market and prices will, therefore, be profitable and will not be restricted, as war profits were.

While the Court below found that debtor's work during the war was under a highly artificial stimulus, it failed to find, and could not find on the findings or the evidence, that there would be any less business after the war or what the business would be.

The refusal to follow the repeated and strong findings that the debtor's prospects are most promising is in con-

flict also with the Congressional Report and the declaration by Congressman Gorski, (a member of the Committee), quoted under (d) of point I, hereinabove, in which it is stated,—

> "We must insist that the owners of these securities now being confiscated should share in the prosperity which has come as a result of the war and in that which necessarily will follow in rebuilding the nation's industries."

Moreover, as the findings as to prospects were approved by the trial judge, the Court below had no jurisdiction to find in conflict with them or to ignore them, but was bound by them (3 Am. Jur. 481; 5 C. J. S. 777).

The ground that debtor had an unusually favorable tax situation in 1943 is also untenable; if, instead of being exempt from Federal tax it had been obliged to pay at the legal rate, its tax would have been $70,000, but as it earned $151,000 it would still have had left over $80,000, and as the dividends on the $400,000 of preferred stock would amount to only $24,000 there would have been an excess of nearly $60,000 to apply on the principal of the debts.

The controlling importance of valuing on earnings instead of on part only of the physical assets is demonstrated by the fact that the net earnings for the past two years averaged $135,000 per year, and a valuation on earnings would show the value to be $1,350,000 (Puget Sound Power & Light Co. v. Puyallup, 51 F.(2) 688,694), over three times the amount of the debts admitted by the Trustee.

3. The Court below failed to take into consideration the following additional and highly important facts,—

In the first 3½ years of the trusteeship the debtor's assets have grown from $63,909.16 to $329,000, and its debts

have increased only from $331,661.18 to $397,927.61. (O. B. pp. 7 & 9.)

Its cash on hand grew from $118,478.21 in May, 1944, to $260,464.52 of current assets in December, 1944. It requires but $75,000 working capital and it has net cash on hand of $201,860.99.

4. In conflict with the purpose of Congress, the Court below, contrary to the findings and the undisputed evidence, rested its decision on,— (1) the erroneous supposition that the debtor lost money the nine years from 1932 to 1941, whereas the losses were not due to the business but to unfair competition and were, in effect, profit; (2) on erroneously overruling the oft-repeated findings of the Master that the company's outlook is marvelously bright; and (3) on a mistaken statement that, if the debtor had paid the regular Federal tax, in 1943 it would not have had the net income to pay its preferred stock dividends, whereas it had almost 3½ times that amount.

Even if there had been losses in the depression years from 1932 to 1941, they should not have been considered in determining whether to value on earnings, the declared purpose of Congress being as follows:

> "It never was intended that these depression earnings should be used as a measure of earning power and, therefore, a measure of value." (Reed, C. R. Feb. 14, 1945, p. 1124.)

It was error for the Court below to overrule the findings and the evidence approved by the trial judge, and especially so as there was no conflict whatever in the evidence,—

> "Ordinarily findings of a master or referee, having support in the evidence, are, like the verdict of a jury, conclusive on appeal * * *." (5 C. J. S. 777.)

"In most jurisdictions, the finding of a referee, a master, or a commissioner, approved by the trial court, is entitled to the same weight and credit and is as binding as a verdict by a jury or a finding by the court itself * * *." (3 Am. Jur. 481.)

5. The Court below also overruled the findings and the evidence in refusing to value the Stewart-Warner claim.

This claim was one for unfair competition. The record shows,—

"* * * recent decisions on the primary questions involved in that litigation have been favorable to Debtor, and there is every reason to expect there will be a substantial recovery by the Debtor's Trustee in the final stages of that litigation." (Plan, top p. 4.)

"I believe defendant has suffered the amount of damages claimed in the amended counter-claim * * *." ($2,000,000.). (Statement of Atty. for Debtor, App. p. 130a.)

"I am entirely satisfied that we can prove liability up to the hilt * * *." (*id.* 127a.)

"In all infringement suits that have gone to trial, we have secured decisions that Stewart-Warner's patents * * * are either invalid or not infringed." (*id.* 129a.)

The trial judge provided and the Court below approved a direction that the proceeds of recovery on this claim be used to retire the new preferred stock,—to pay the creditors in full,—and for distribution of the remainder to the present preferred and common shareholders (Opinion, pp. 3 & 4),—the necessary inference from this provision being that both courts regard this claim as one in which there will be a recovery sufficient not alone to pay all the debts in full, but to leave a substantial amount for the present stockholders.

The trial court has directed that the Trustee expend the amounts necessary for carrying on this litigation. (Master's Rep. pp. 32 a, 72 a.)

The statement in the plan that there will be a substantial recovery, as the plan is the pleading in the case, is conclusive and cannot be disputed. (Jones on Evidence, 2d Ed. §1045, p. 187.)

Moreover, the whole case was tried on this statement of the Trustee in the plan.

The Court below erroneously extinguished this claim on the ground that,—

> "* * * we have not * * * the faintest notion of the strength of the debtor's case nor the defendant's defense" (Opinion p. 4),

whereas it had all the evidence quoted above,—the opinion of the attorney in the case and the statement of the Trustee in the plan. (Cons. Rock Co. v. DuBois, 312 U. S. 510, 522, 523, *In re* Western Pac. R. Co., 124 F. (2d) 136, 138, 139.)

The claims not disputed by the Trustee amount to $397,927.61. The Master found a part of the physical property (not including the Stewart-Warner claim nor the patent) worth $327,000, making the excess of debts over value of part of physical assets $70,927.61.

The patent is concededly worth $40,000, Brynoldt's invalid rental claim is $29,316, making together $69,316. So there is really no difference between the value of part of the physical assets and the admitted debts. Moreover, the Stewart-Warner claim, on the evidence as stated above, is

surely worth several times the amount of any possible difference.

6. The Court below also erroneously refused to value a coupler patent worth $40,000,—an item of property to which Brynoldt attempted to acquire title through his unfounded claim to all of the debtor's property,—worth on earnings $1,500,000,—for a loan of $23,500,—an unconscionable bargain, from which equity will relieve on account of the advantage taken by him and hardship suffered by debtor. (U. S. v. Bethlehem Steel, 315 U. S. 328, 329.) The patent should have been valued and not "extinguished". (Consolidated Rock Products Co. v. DuBois, 312 U. S. 510.)

7. The Court also erroneously refused to value a claim against one Brynholdt for slander of title in claiming ownership of all debtor's property, in an unjust effort to convert a $23,500 loan into such ownership, part of the physical items of this property being worth $327,000, and all of it on earnings over $1,500,000 (O. B. pp. 2 & 3). There could be no finding of value except on a complete appraisal. (Cons. Rock Co. v. DuBois, *supra; in re* Western Pac. R. Co., *supra.*)

IV.

The decision below is most unfair, unjust and inequitable, in that,

1. It allows one Brynoldt a claim for rent of debtor's property of $29,316, although the Trustee concedes that he never owned the property (O. B. p. 22),—a wholly baseless claim.

2. Yet Brynoldt, who attempted to secure $327,000 worth of physical assets,—to say nothing of its earning value of

$1,500,000,—for $23,500, together with his attorney and the Trustee, a brother of his son-in-law, are made three of the directors of the new corporation, and Brynoldt alone, of all the creditors, is to be made a large cash payment.

3. The provision of the plan that the creditors shall be paid in full from the recovery in the Stewart-Warner suit and then be given all debtor's property, is unconscionable and indefensible. (O. B. p. 23.)

The statement of Congressman Hobbs, the author of the House bill, is peculiarly apposite to this unconscionable and indefensible provision of the plan,—

> "The purpose of the bankruptcy act, particularly of sec. 77, was to relieve debtors of some of their burdens, not of all of their property." (Hobbs, C. R. Feb. 14, 1945, p. 1126.)

4. Under the plan the stockholders remain the owners of the Stewart-Warner claim,—by far the largest asset of the corporation,—subject only to payment of the creditors, but exclusive control of the litigation is given to the trustee, with no privilege to the stockholders to see that their rights are protected and they justly feel, from the advocacy of the invalid Brynoldt rental claim by the trustee and the favoritism shown him, distrustful of his fairness toward the stockholders, and this provision is inequitable and unjust.

Conclusion.

As shown above, Congress has repeatedly declared that its intention and purpose is that stockholders shall continue in business so that manufacturers may obtain from the public the capital necessary to continue them in operation through reliance on the security of their loans, and

to avoid and minimize depressions and to keep labor employed and has diligently labored to accomplish this beneficient end through the appointment of a committee which has been tireless in this work and by providing for loans to small business. There can be no greater public purpose than this. To accomplish the end sought, the co-operation of the Courts with the Congress is necessary. The decision of the Court below is plainly in conflict with its oft-repeated declarations of its purpose by Congress.

The effort should have been in accord with the purpose of Congress to continue the stockholders in business, and this would have resulted from performance of its duty by the Court below to value debtor's plant on earnings,—a valuation required on debtor's whole history, on its being able to earn enough so that it *made* and through unfair competition in nine years lost $2,000,000.; and has made over $196,000 in three years of the expensive and inefficient management of a trustee; has earned an average of $135,000 per year for the past two years; and has undisputedly and on the findings and evidence the brightest kind of prospects for large earnings in the future. These prospects show that debtor's business will be greater than during the war period, which answers the contention of the Court below that the recent earnings should not be considered because of war conditions. Moreover, Congress has itself declared that the post war period is to have a continuance of war prosperity and that the rights of stockholders should be considered with reference to such conditions. (See subhead (d) of point I, p. 11, hereinabove.) And while the Court below laid stress on the debtor's favorable tax situation for the last two years, the tax situation for all corporations is, the court will take judicial notice, to be greatly improved over the provisions of the present tax law.

So far as counsel is able to find, the declarations by Congress of its purpose to save the common stockholder and continue business have never been called to the attention of the Courts and there has been no decision by this or any of the lower Courts in view of these declarations.

> "* * * the primary rule of construction of statutes is to ascertain and declare the intention of the legislature, and carry such intention into effect to the fullest degree." (50 Am. Jr. §223, pp. 201, 202.)

An opinion by this Court that the rights of common stockholders must be considered with the aid of the favorable intent of Congress, would be of incalculable value to the business world. To allow the opinion below to stand would beget doubt and uncertainty by investors as to the value of common stock, and would have just the opposite effect of that intended by Congress. It would, to a very considerable degree, defeat the intention of Congress and such a construction should not be adopted. (*id.* pp. 202, 203.) The extent of the harm which would result from allowing the decision below to stand, in view of the debtor being solvent and of the many unjust and unfair provisions of the plan, cannot be estimated, but would, beyond doubt, be very great.

For all these reasons, it is respectfully urged that a rehearing and certiorari should be granted.

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